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West Shore Bank Business Symposium

Tax Update

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Disclosure

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Tax Developments in 2012

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Tangible Asset Regulation

- Treasury Department has issued new rules regarding Capitalization and Deduction of Expenditures related to Tangible Property effective for taxable years beginning on or after January 1, 2012
- How does this affect the businesses? – It gives clarity to taxpayers in determining whether expenditures related to tangible assets should be expensed during the year or need to be capitalized and depreciated

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Tangible Asset Regulations

- Regulations cover four main subject matter areas
  - Material and Supplies
    - Timing of deducting costs
    - Elective capitalization
    - Optional method for rotable spare parts
  - Acquisition of Tangible Property
    - Determination of what costs need to be capitalized
    - The most significant element relates to the de minimis rule
  - Improvements to Tangible Property
    - Defines unit of property for applying the betterment and restoration standards
    - Creates a safe harbor for routine maintenance
    - Provides guidance regarding what constitutes a betterment or restoration of property
    - As part of the restoration rules, illustrates what is considered a major component
    - Provides guidance to determine when the property has been adapted for a new or different use
  - Disposition of Tangible Property
    - Provides framework for dispositions of components of property
    - Expands the use of general asset accounts for purpose of component dispositions

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Tangible Asset Regulations

- Transition Rules
  - Generally, the temporary regulations are effective for tax years beginning on or after January 1, 2012 and will impact the treatment of costs during 2012
  - A change to adopt the regulations will require the filing of a Form 3115 filed under automatic consent provisions and the rule may apply retrospectively
  - Some of the provisions may require changing book accounting policies and/or book accounting methods to align with newly required tax methods
  - Rev. Proc. 2012-19 and Rev. Proc. 2012-20 provide the accounting method change procedures for taxpayers to comply with the new regulations
- Next Steps
  - Evaluate how the regulations may impact the accounting for materials and supplies, improvements to property and routine maintenance as it relates to capitalizing or deducting those costs
  - Determine how the de minimis rule might affect your capitalization threshold and the accounting for costs deducted under that policy
  - Determine whether and to what extent your business currently accounts for dispositions and what the appropriate method(s) might be under the temporary regulations

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Form 8937 – Reporting for Corporate Actions

- New information reporting requirements for corporate transactions under §6045B. Applies to C corporations and S corporations. Does not apply to partnerships
- Reporting done on Form 8937
- Requires reporting of certain organizational actions
- Includes actions such as stock splits, stock distributions, recapitalizations, redemptions, distributions not taxed as dividends and mergers and acquisitions in which stock or a combination of stock and cash is issued

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Form 8937 – Reporting for Corporate Actions

- Reporting mandatory for corporate transactions occurring on or after January 1, 2011
- IRS Form 8937 must be filed with the IRS by the earlier of:
  - 45 days after the date of the action, or
  - January 15th of the year following the calendar year the action occurred
- Reports must be provided to shareholders by January 15th of the year following the calendar year of the action
- A corporation can satisfy the reporting requirements by posting Form 8937 in a readily accessible format in an area of its primary website dedicated to this purpose for a period of 10 years

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Form 8937 – Reporting for Corporate Actions

- Reporting requirements
  - IRS released Form 8937 on January 5, 2012
  - Due date for 2011 Form 8937 delayed until January 17, 2012
  - Penalties for failure to file are up to $100 per shareholder and IRS statement not filed (with a cap of $1.5 million each for shareholder/IRS statements not filed)
- Application to S Corporations
  - S Corporations can satisfy the Form 8937 filing requirement by timely filing tax return with item reported on Schedule K-1
    - E.G. – if an ordinary distribution is reported as code D, line 16 on Schedule K-1, the reporting requirement is considered met
    - If a transaction is not typically reported on Schedule K-1 (e.g. a recapitalization affecting stock basis), add a footnote with the information request by Form 8937
      - It is not necessary to complete Form 8937 – you can include a footnote to the Schedule K-1 with information required by Form 8937

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Form 8938 – New Foreign Financial Interest Reporting for Individuals

- Individuals with any of the following items must file Form 8938 with their 2011 tax return:
  - Any depositary or custodial account maintained by a foreign financial institution;
  - Stocks or securities issued by or any other interest in a foreign entity;
  - Any financial instrument or contract with an issuer or counterparty other than a U.S. person; or
  - Other foreign financial assets
- Filing not required if you do not otherwise have a Form 1040 filing requirement
- Reporting threshold ($$ value of assets)

Single/MFS	MFJ
U.S.: $50K last day, $75K anytime	U.S.: $100K last day, $150K anytime
Abroad: $200K last day, $300K anytime	Abroad: $400K last day, $600K anytime

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Form 8938 – New Foreign Financial Interest Reporting for Individuals

- Once threshold exceeded, all foreign assets included
- Value is maximum value at any point during the year
- Penalty for not filing - $10,000
  - Underpayment of tax due to failed disclosure has 40% penalty
- Still required to file FBAR

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FBAR Requirements

- Form TD F 90-22.1 (FBAR)
- Due June 30th each year for prior year
- File Form if:
  - Have financial interest or signature authority
  - Aggregate value of foreign accounts exceeds $10,000 at any time during year
- Failure to file, penalty $10,000 per year

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S Corporation Shareholder Basis

- Loss deductions limited to shareholder basis
- Basis generally:
  - Capital invested
  - Invested earnings
  - Loans by shareholder to S corporation
  - Reduced by distributions and deducted losses
- Maguire V. Comr., T.C. Memo 2012 – 160 (6/6/12)
  - Two related S corporations
  - One with basis, one without
  - Profitable S corporation can distribute assets that can be used to create basis in loss S corporation
  - Must be bona fide loan

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Unearned Income Medicare Tax

- Effective for years beginning after December 31, 2012
- Applies to individuals, estates and trusts
- Tax rate equals 3.8%
- Tax calculations:
  - 3.8% of the lesser of:
    - Net investment income
    - Modified adjusted gross income in excess of:
      - $250,000 if married filing jointly
      - $125,000 if married filing separately
      - $200,000 if filing as a single individuals
      - $12,000 for trusts and estate

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Impact of Expiring Bush Era Tax Cuts

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Provision/Benefit	Current	2013
Individual Income Tax Rates	10%/15%/25%/28%/ 33%/35%	15%/28%/31%/ 36%/39.6%
Standard Deduction	$11,900	$9,950
Cap. Gains Tax Rate	15% (0% for 10-15%	20% Tax bracket)
Dividends	15%	Ordinary Income Tax rates
Itemized Deduction Limits	No Income Limit	Will be reduced by 3% of the amount by which the AGI exceeds the applicable threshold
Personal Exemption Phase Out	No Income Restriction	Will be reduced by 2% for each $2,500 by which the AGI exceeds applicable thresholds
Estate Tax	Exemption is $5,120,000 and top rate is 35%	Exemption will be $1,000,000 and top tax rate 55%

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Provision/Benefit	2011	2012	2013 & beyond
Bonus Depreciation	100%	50%	0%
Sec 179 Limit	$500,000/ $2,000,000	$125,000/ $500,000	$25,000/ $200,000
Elect to Accelerate AMT Credits instead of Addn. 1st Year Depreciation	Available	Available	Expired

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Year End Tax Planning

- Consider Uncertainty
- Accelerate Income/Defer Deductions
  - Individuals – Yes
  - Corporations – No?
- Accelerate Dividend Payments
- Capital Gain/Loss Planning
- Estate and Gift
  - Exemption Utilization
  - Taxable Gifts

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